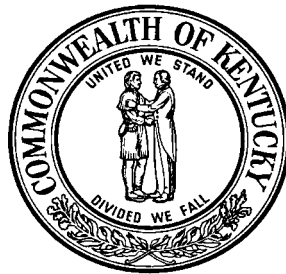


**REPORT OF THE AUDIT OF THE
KNOTT COUNTY
CLERK**

**For The Year Ended
December 31, 2002**



**CRIT LUALLEN.
AUDITOR OF PUBLIC ACCOUNTS
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CRIT LUALLEN
Auditor of Public Accounts

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Robbie Rudolph, Secretary
Finance and Administration Cabinet
Honorable Donnie Newsome, Knott County Judge/Executive
Honorable Ken Gayheart, Knott County Clerk
Members of the Knott County Fiscal Court

The enclosed report prepared by Ross & Company, PLLC, Certified Public Accountants, presents the statement of receipts, disbursements, and excess fees of the County Clerk of Knott County, Kentucky, for the year ended December 31, 2002.

We engaged Ross & Company, PLLC to perform the financial audit of this statement. We worked closely with the firm during our report review process; Ross & Company, PLLC evaluated the Knott County Clerk's internal controls and compliance with applicable laws and regulations.

Respectfully submitted,

A handwritten signature in cursive script, reading "Crit Luallen".

Crit Luallen
Auditor of Public Accounts

Enclosure



**REPORT OF THE AUDIT OF THE
KNOTT COUNTY
CLERK**

**For The Year Ended
December 31, 2002**

ROSS & COMPANY, PLLC
Certified Public Accountants
800 Envoy Circle
Louisville, KY
Telephone (502) 499-9088
Facsimile (502) 499-9132

EXECUTIVE SUMMARY

AUDIT EXAMINATION OF THE KNOTT COUNTY CLERK

**For The Year Ended
December 31, 2002**

Ross & Company, PLLC has completed the Knott County Clerk's audit for the year ended December 31, 2002. We have issued an unqualified opinion on the financial statement taken as a whole. Based upon the audit work performed, the financial statement is presented fairly in all material respects.

Financial Condition:

Excess fees increased by \$6,951 from the prior calendar year, resulting in excess fees of \$15,149 as of December 31, 2002. Revenues increased by \$113,219 from the prior year and disbursements increased by \$106,268.

Report Comments:

- Lacks Adequate Segregation Of Duties
- The County Clerk Should Require Depository Institutions To Pledge Or Provide Sufficient Collateral To Protect Deposits

Deposits:

On April 2, 2002, \$35,705 of the Knott County Clerk's deposits of public funds were uninsured and unsecured by bank securities or bonds.

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To the People of Kentucky
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Independent Auditor's Report

We have audited the accompanying statement of receipts, disbursements, and excess fees of the County Clerk of Knott County, Kentucky, for the year ended December 31, 2002. This financial statement is the responsibility of the County Clerk. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for County Fee Officials issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the County Clerk's office prepares the financial statement on a prescribed basis of accounting that demonstrates compliance with the modified cash basis and laws of Kentucky, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statement referred to above presents fairly, in all material respects, the receipts, disbursements, and excess fees of the County Clerk for the year ended December 31, 2002, in conformity with the modified cash basis of accounting.

In accordance with Government Auditing Standards, we have also issued our report dated November 25, 2003, on our consideration of the County Clerk's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Robbie Rudolph, Secretary
Finance and Administration Cabinet
Honorable Donnie Newsome, Knott County Judge/Executive
Honorable Ken Gayheart, Knott County Clerk
Members of the Knott County Fiscal Court

Based on the results of our audit, we have presented the accompanying comments and recommendations, included herein, which discusses the following report comments:

- Lacks Adequate Segregation Of Duties
- The County Clerk Should Require Depository Institutions To Pledge Or Provide Sufficient Collateral To Protect Deposits

Respectfully submitted,

A handwritten signature in cursive script that reads "Ross & Company".

Ross & Company, PLLC

Audit fieldwork completed -
November 25, 2003

KNOTT COUNTY
 KEN GAYHEART, COUNTY CLERK
STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES

For The Year Ended December 31, 2002

Receipts

State Fees For Services	\$	8,173
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Fiscal Court		17,052
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Licenses and Taxes:

Motor Vehicle-

Licenses and Transfers	\$	462,619
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Usage Tax		966,978
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Tangible Personal Property Tax		797,647
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Licenses-

Fish and Game		10,290
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Marriage		5,175
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Deed Transfer Tax		19,415
-------------------	--	--------

Delinquent Tax	135,093	2,397,217
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Fees Collected for Services:

Recordings-

Deeds, Easements, and Contracts	\$	14,891
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Real Estate Mortgages		18,616
-----------------------	--	--------

Chattel Mortgages and Financing Statements		54,667
--	--	--------

All Other Recordings		17,993
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Charges for Other Services-

Candidate Filing Fees	2,270	108,437
-----------------------	-------	---------

Interest Earned		1,437
-----------------	--	-------

Total Receipts	\$	2,532,316
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The accompanying notes are an integral part of this financial statement.

KNOTT COUNTY
 KEN GAYHEART, COUNTY CLERK
 STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES
 For The Year Ended December 31, 2002
 (Continued)

Disbursements

Payments to State:

Motor Vehicle-

Licenses and Transfers \$ 376,324

Usage Tax 935,899

Tangible Personal Property Tax 349,769

Licenses, Taxes, and Fees-

Fish and Game 10,067

Delinquent Tax 19,417

Legal Process Tax 14,476

Candidate Filing Fees 925 \$ 1,706,877

Payments to Fiscal Court:

Tangible Personal Property Tax \$ 84,387

Delinquent Tax 13,145

Deed Transfer Tax 18,444 115,976

Payments to Other Districts:

Tangible Personal Property Tax \$ 331,559

Delinquent Tax 63,871 395,430

Payments to Sheriff

3,205

Payments to County Attorney

17,646

Operating Disbursements and Capital Outlay:

Personnel Services-

Deputies' Salaries \$ 144,616

Employee Benefits-

Employer's Share Social Security 15,872

Employer's Share Retirement 14,268

Contracted Services-

Tax Bill Preparation 2,780

Legal and Accounting 4,650

Other Charges-

Bank Charges 46

Conventions and Travel 3,403

Dues 450

The accompanying notes are an integral part of this financial statement.

KNOTT COUNTY
 KEN GAYHEART, COUNTY CLERK
 STATEMENT OF RECEIPTS, DISBURSEMENTS, AND EXCESS FEES
 For The Year Ended December 31, 2002
 (Continued)

Disbursements (Continued)

Operating Disbursements and Capital Outlay: (Continued)

Other Charges- (Continued)

Postage	\$	5,980	
Refunds		5,470	
Contract Services		2,115	
Miscellaneous		<u>9,559</u>	\$ 209,209

Total Disbursements			\$ <u>2,448,343</u>
---------------------	--	--	---------------------

Net Receipts			\$ 83,973
Less: Statutory Maximum			<u>62,259</u>

Excess Fees			\$ 21,714
Less: Expense Allowance	\$	3,600	
Training Incentive Benefit		<u>2,965</u>	<u>6,565</u>

Excess Fees Due County for 2002			\$ 15,149
Deed Transfer Overpayment Reclassed as Excess Fees - April 7, 2002			127
Payments to County Treasurer - March 18, 2003			<u>16,011</u>

Excess Fees Overpaid at Completion of Audit			<u>\$ (989)</u>
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KNOTT COUNTY
NOTES TO FINANCIAL STATEMENT

December 31, 2002

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

A fee official uses a fund to report on the results of operations. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fee official uses a fund for fees to account for activities for which the government desires periodic determination of the excess of receipts over disbursements to facilitate management control, accountability, and compliance with laws.

B. Basis of Accounting

The financial statement has been prepared on a modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under this basis of accounting, certain receipts and certain expenditures are recognized as a result of accrual at December 31, 2002.

The measurement focus of a fee official is upon excess fees. Remittance of excess fees is due to the County Treasurer in the subsequent year.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the County Clerk's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Employee Retirement System

The county officials and employees have elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a multiple-employer public retirement system that covers all eligible full-time employees. Benefit contributions and provisions are established by statute. Nonhazardous covered employees are required to contribute 5.0 percent of their salary to the plan. The county's contribution rate for nonhazardous employees was 6.41 percent for the first six months and 6.34 percent for the last six months of the calendar year.

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65.

KNOTT COUNTY
 NOTES TO FINANCIAL STATEMENT
 December 31, 2002
 (Continued)

Note 2. Employee Retirement System (Continued)

Historical trend information pertaining to CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report which is a matter of public record.

Note 3. Deposits

The County Clerk maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the County Clerk and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. The County Clerk entered into a written agreement with the depository institution and met requirements (a), (b), and (c) stated above. However, as of April 2, 2002, the collateral and FDIC insurance together did not equal or exceed the amount on deposit, leaving \$35,705 of public funds uninsured and unsecured.

The county official's deposits are categorized below to give an indication of the level of risk assumed by the county official at year-end or as of April 2, 2002.

	<u>Bank Balance</u>
FDIC insured	\$ 100,000
Collateralized with securities held by pledging depository institution in the county official's name	200,000
Uncollateralized and uninsured	<u>35,705</u>
Total	<u><u>\$ 335,705</u></u>

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COMMENTS AND RECOMMENDATIONS

KNOTT COUNTY
KEN GAYHEART, COUNTY CLERK
COMMENTS AND RECOMMENDATIONS

For The Year Ended December 31, 2002

STATE LAWS AND REGULATIONS:

The County Clerk Should Require Depository Institutions To Pledge Or Provide Sufficient Collateral To Protect Deposits

On April 2, 2002, \$35,705 of the County Clerk's deposits of public funds in depository institutions were uninsured and unsecured. According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with Federal Deposit Insurance Corporation insurance, equals or exceeds the amount of public funds on deposit at all times. We recommend that the County Clerk require the depository institution to pledge or provide collateral in an amount sufficient to secure deposits of public funds at all times.

County Clerk's Response: None

INTERNAL CONTROL - REPORTABLE CONDITION AND MATERIAL WEAKNESS:

Lacks Adequate Segregation Of Duties

We recognize the extent of segregation of duties is a judgment established by management. We also recognize this judgment is affected by certain circumstances beyond the elected officials control such as functions prescribed by statutes and regulations, and by budgetary constraints. Due to limited staff, a proper segregation of duties may be impossible. We recommend that the Clerk implement compensating controls to offset this internal control weakness. Examples of compensating controls are: 1) the official recounting and depositing cash; 2) the official agreeing daily AVIS computer totals to receipts for usage tax, license fees, and tangible personal property taxes; and the Clerk reconciling monthly reports to source documents and receipts and disbursement ledgers. The lack of adequate segregation of duties is hereby noted as a reportable condition pursuant to professional auditing standards. We believe this reportable condition as described above is a material weakness.

County Clerk's Response: None

PRIOR YEAR:

None

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REPORT ON COMPLIANCE
AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF THE FINANCIAL STATEMENT
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

ROSS & COMPANY, PLLC
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To the People of Kentucky
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Members of the Knott County Fiscal Court

Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards

We have audited the statement of receipts, disbursements, and excess fees of the Knott County Clerk for the year ended December 31, 2002, and have issued our report thereon dated November 25, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Knott County Clerk's financial statement for the year ended December 31, 2002, is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under Government Auditing Standards and which is described in the accompanying comments and recommendations.

- The County Clerk Should Require Depository Institutions To Pledge Or Provide Sufficient Collateral To Protect Deposits

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Knott County Clerk's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. A reportable condition involves matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. A reportable condition is described in the accompanying comments and recommendations.

- Lacks Adequate Segregation Of Duties

Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards
(Continued)

Internal Control Over Financial Reporting (Continued)

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition described above to be a material weakness.

This report is intended solely for the information and use of management and is not intended to be and should not be used by anyone other than the specified party.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Ross & Company", written in a cursive style.

Ross & Company, PLLC

Audit fieldwork completed -
November 25, 2003

